

UNITED STATES BANKRUPTCY COURT

DISTRICT OF NEVADA

LAS VEGAS, NEVADA

In re: THE RHODES COMPANIES,) E-Filed: 10/04/11
LLC,)
Debtor.) Case No.
BK-S-09-14814-LBR
Chapter 11

TRANSCRIPT OF PROCEEDINGS
OF

HEARING RE: MOTIONS

VOLUME 1

BEFORE THE HONORABLE LINDA B. RIEGLE
UNITED STATES BANKRUPTCY JUDGE

Tuesday, September 27, 2011

10:30 a.m.

Court Recorder: Deborah Hemstreet

Proceedings recorded by electronic sound recording;
transcript produced by transcription service.

1 APPEARANCES:

2 For the Reorganized
3 Debtor:ABID QURESHI, ESQ.
MEREDITH A. LAHAIE, ESQ.
Akin, Gump, Strauss, Hauer & Feld, LLP
One Bryant Park
New York, New York 100365 HOWARD B. JACOBSON, ESQ.
Akin, Gump, Strauss, Hauer & Feld, LLP
1333 New Hampshire Avenue, N.W.
Washington, D.C. 20036
7 (Telephonic)8 SHIRLEY S. CHO, ESQ.
Pachulski, Stang, Ziehl & Jones, LLP
9 10100 Santa Monica Boulevard
Thirteenth Floor
10 Los Angeles, California 90067
11 (Telephonic)SHLOMO S. SHERMAN, ESQ.
12 Kolesar & Leatham, Attorneys At Law
400 South Rampart Boulevard
13 Suite 400
Las Vegas, Nevada 8914514 For the United States
15 of America Internal
Revenue Service:VIRGINIA CRONAN LOWE, ESQ.
United States Department of Justice
Tax Division
16 Ben Franklin Station
Post Office Box 683
17 Washington, D.C. 2004418 For The Litigation
Trust of the
19 Rhodes Companies, LLC:ERIC D. MADDEN, ESQ.
Diamond McCarthy, LLP
1201 Elm Street
Suite 3400
20 Dallas, Texas 75270
(Telephonic)21 MICHAEL YODER, ESQ.
Diamond McCarthy, LLP
Two Houston Center
22 909 Fannin Street
Fifteenth Floor
23 Houston, Texas 77010
24 (Telephonic)
25

1 APPEARANCES (Cont.):

2 For James Rhodes: DAVID R. HAGUE, ESQ.
3 Fabian & Clendenin
4 215 South State Street
Suite 1200
Salt Lake City, Utah 84111

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1 (Court convened at 10:42:01 a.m.)

2 THE CLERK: Bankruptcy court is now in session.

3 (Colloquy not on the record.)

4 THE COURT: Be seated.

5 (Colloquy not on the record.)

6 THE COURT: All right. Rhodes.

7 Appearances, please.

8 MR. QURESHI: Good morning, your Honor. For the
9 record, Abid Qureshi, Akin, Gump, Strauss, Hauer & Feld, on
10 behalf of the reorganized debtors. With me in the courtroom is
11 Meredith Lahaie, and on the phone also from Akin, Gump is
12 Howard Jacobson.

13 THE COURT: Okay.

14 MS. LOWE: Virginia Lowe with the Department of
15 Justice representing the United States.

16 MR. SHERMAN: Good morning, your Honor.
17 Shlomo Sherman, local counsel for the reorganized debtors.

18 THE COURT: All right. All right. Should we do the
19 IRS claim first?

20 MR. QURESHI: Sure, your Honor. And, your Honor,
21 also on the phone is Shirley Cho of Pachulski, Stang also on
22 behalf of the reorganized debtors.

23 MR. MADDEN: Your Honor --

24 MR. QURESHI: (Indiscernible).

25 MR. MADDEN: -- you also have --

1 THE COURT: Oh, sorry.

2 MR. QURESHI: I'm sorry.

3 MR. MADDEN: Your Honor, you also have Eric Madden
4 and Michael Yoder on the phone for the Litigation Trust.

5 THE COURT: Okay. Thank you.

6 MR. QURESHI: Okay.

7 THE COURT: Okay.

8 MR. QURESHI: And --

9 THE COURT: First, we have the objection to the IRS
10 claim.

11 MR. QURESHI: Yes, your Honor. If I may proceed,
12 your Honor, first, just by way of background with respect to
13 this claim?

14 So what the IRS claim is about is an attempt by the IRS to
15 recover millions of dollars in avoided tax liability from a tax
16 fraud that was committed about a decade ago, and this is a tax
17 fraud, your Honor, that the reorganized debtors and, in
18 particular, Bravo, which is the debtor entity against whom the
19 claim was filed had nothing to do with and nor is it alleged
20 that Bravo was in any way implicated a part of this fraudulent
21 scheme to defraud the IRS.

22 What the IRS is seeking to do, your Honor, we think is try
23 to tag the debtors with liability with this scheme and to do so
24 inappropriately and without evidence. Let me start with the
25 genesis of the claim itself.

1 Bravo, rather, was a subsidiary in the Rhodes
2 organization, and the function of that entity was to provide
3 framing services. This was the subsidiary through which
4 laborers built the frame.

5 Your Honor, I apologize. I just got a note that the
6 people on the phone cannot hear anything.

7 THE COURT: Okay.

8 MS. CHO: No. We're on Abid.

9 MR. QURESHI: Oh, you are? Okay. Thank you. I
10 apologize, your Honor. So during the time period from 2000
11 until 2003 -- and that, your Honor, is the period of time
12 during which these tax liabilities were allegedly incurred --
13 Bravo hired a subcontractor through which it received laborers
14 that were necessary to complete the framing work that was going
15 on during the housing boom, and I'll come back to that in a
16 little bit more detail.

17 The company that was retained as a subcontractor was
18 Union Pacific Construction, and I will refer to them,
19 your Honor, as UPC.

20 So in 2009, the owner of UPC, a gentleman by the name of
21 Robert Kahre -- and I apologize if I'm mispronouncing his
22 name -- he and a number of his associates were convicted in a
23 criminal tax-fraud case by the district court here in
24 Las Vegas, and he I believe is serving a sentence of somewhere
25 in the order of 15 years, and a number of his associates

1 involved in the scheme are also serving jail sentences.

2 Now, the scheme that was run by UPC was as follows,
3 your Honor: Apparently, UPC provided among other things
4 payroll services to a number of construction companies in the
5 Las Vegas area.

6 And what Mr. Kahre did through this scheme was he claimed
7 to pay the employees of these various construction companies in
8 gold and silver coins which the employees would then
9 immediately exchange for cash, and what was reported to the IRS
10 was the face amount of the gold and the silver coins which was
11 approximately one-eighth the value of the cash that those
12 employees actually received.

13 Now, the IRS has alleged that the UPC provided those same
14 fraudulent payroll services to Bravo, and so what it's seeking
15 to recover from the reorganized debtors is the following,
16 your Honor: A priority claim totalling approximately
17 1.32 million dollars.

18 Now, importantly, that 1.32 breaks down into approximately
19 \$879,000 in unpaid taxes and \$446,000 in penalty interest which
20 I believe runs up to the petition date and, in addition, an
21 unsecured claim in the total amount of 2.56 million dollars,
22 and that claim, your Honor, is 432,000 in principal and 849,000
23 approximately in penalty interest.

24 Now, the legal issue before the Court, your Honor, I think
25 it's actually a fairly straightforward one, the reorganized

1 debtor's claim and our objection and with a supporting
2 affidavit that Bravo hired UPC as a subcontractor.

3 There is no dispute, your Honor, that if that is correct,
4 if, indeed, UPC was hired as a subcontractor, Bravo bears no
5 responsibility for any taxes that UPC may have failed to pay.

6 Now, on the other hand, what the IRS claims is that Bravo
7 hired UPC not as a subcontractor, but, instead, as a payroll
8 servicer. That Bravo remained the employer of its laborers
9 and, therefore, remained liable to remit the appropriate
10 payroll taxes to the IRS.

11 And so the legal question that I think is ultimately
12 determinative of this claim is did Bravo retain UPC as a
13 subcontractor or did Bravo retain UPC as a payroll servicer.

14 THE COURT: Why isn't that a factual question as
15 opposed to a legal question?

16 MR. QURESHI: I apologize, your Honor. It is a
17 factual question which is determinative of the legal issue of
18 whether they have a valid claim. That is absolutely correct,
19 so let's start with the proof of claim filed by the IRS.

20 THE COURT: Well, if it's a factual question, how do
21 we get anyplace today?

22 MR. QURESHI: Well, here's how we get anyplace today,
23 your Honor. We have submitted in connection with our objection
24 an affidavit. The affidavit is from a Mr. Dean Griffiths
25 (phonetic). He was a former employee of Bravo during the

1 relevant time period here, and his declaration, your Honor, is
2 at Docket No. 1532.

3 He was employed by Bravo from 1996 through 2004, and among
4 the titles that he held during his employment at Bravo was
5 general manager and general superintendent.

6 THE COURT: But why? You're not going to dispute a
7 material factual issue here --

8 MR. QURESHI: Respectfully, your Honor --

9 THE COURT: -- because you're, in essence, asking me
10 to discern (indiscernible) --

11 MR. QURESHI: I --

12 THE COURT: -- a summary judgment.

13 MR. QURESHI: Your Honor, I actually don't think it's
14 disputed, and let me explain. So we've submitted his
15 declaration. In his declaration, Mr. Griffiths says very
16 clearly and very directly Bravo hired UPC as a subcontractor.

17 Now, the IRS I believe has no objection to the
18 admissibility of this declaration. It has not requested the
19 presence of Mr. Griffiths to be cross-examined, and so I don't
20 believe that there is any contrary evidence to dispute what
21 Mr. Griffiths has said.

22 What the IRS offers, your Honor, is trial transcripts from
23 the underlying criminal proceeding. And through those trial
24 transcripts, the IRS believes that it can establish that Bravo,
25 in fact, retained UPC as a payroll servicer.

1 But, in fact, your Honor, the trial transcripts, all of
2 them -- and set to the side for a moment their admissibility
3 because, in fact, I don't think they're admissible here.

4 But setting that to the side, those trial transcripts
5 nowhere say that Bravo retained UPC as a payroll servicer.
6 That is an implication that the IRS asks this Court to draw
7 from those transcripts, and we don't believe it can do so. We
8 don't believe that those transcripts come even close to
9 establishing that.

10 And if I might for a moment, your Honor, address on the
11 assumption that the IRS will seek to offer those transcripts
12 into evidence, I think they are plainly inadmissible.

13 Let's start with testimony provided in another proceeding
14 is hearsay. It's clearly hearsay under the federal rules, so
15 the next question is is there an exception through which that
16 hearsay becomes admissible in these proceedings.

17 The Federal Rule of Evidence 804(b)(1) is the rule that we
18 look to to see if there is an exception to the hearsay rule
19 that applies here. There are two components to that exception
20 that must be met for these transcripts even to be admissible.

21 First, your Honor, the witness has to be unavailable,
22 and --

23 THE COURT: Well, that's pretty clear.

24 MR. QURESHI: Well, actually, that's what I thought,
25 too, your Honor. There's actually case law that says that

1 because a witness is incarcerated does not conclusively
2 establish that the witness is unavailable.

3 THE COURT: Well, he's not in this jurisdiction, is
4 he?

5 MR. QURESHI: I don't know. He was convicted in
6 Las Vegas. I don't know where he is incarcerated, but --

7 THE COURT: Well, there's no federal prison in
8 Nevada, so --

9 MR. QURESHI: Well, there's the answer, then. I
10 guess he's not in this jurisdiction, but that doesn't matter,
11 your Honor, because the second part of the test clearly cannot
12 be met.

13 The second part of the test under 804(b)(1) for this
14 testimony to be admissible in these proceedings is that the
15 party against whom the testimony is being offered, in this
16 case, the reorganized debtors, must have had an opportunity to
17 cross-examine the witness in whatever that prior proceeding
18 was.

19 Well, we weren't there, your Honor, during the criminal
20 trial. We had no opportunity to question any of the witnesses
21 whose trial testimony is now being offered in these
22 proceedings.

23 THE COURT: Well, were any of the Rhodes entities
24 indicted or --

25 MR. QURESHI: No.

1 THE COURT: All right.

2 MR. QURESHI: Your Honor, the Rhodes entities --
3 there is no allegation that the Rhodes entities were in any way
4 involved.

5 And so what your Honor respectfully is left with in terms
6 of a factual record is a proof of claim filed by the IRS which
7 does nothing, your Honor, except for lay out in a schedule
8 amounts owed and dates those obligations were incurred.

9 It says nothing about the question of whether Bravo
10 retained UPC as a payroll servicer, and it has no documentary
11 attachment that would suggest that that is the case.

12 On the other hand, in our objection, we again have the
13 declaration of Mr. Griffiths to which there is no objection.
14 He is competent to testify on the issue. He was the general
15 manager at the time.

16 And he has stated unequivocally that Bravo retained UPC as
17 a contractor. That it did so, your Honor, because this
18 occurred during the housing boom when there were more homes
19 that required framing than Bravo was able to keep up with.

20 And given as he explains in his declaration the
21 administrative burden of hiring additional employees and
22 dealing with the paperwork that that involves, Bravo elected to
23 effectively farm that out to an independent contractor, in this
24 case, UPC, and so we don't think, your Honor, that there really
25 is a factual dispute.

1 Now, I'm prepared if your Honor would like to go through
2 in much more detail the specific sections of the trial
3 testimony to which the IRS points to explain to your Honor why
4 we don't think that raises even a suggestion that Bravo was
5 retaining UPC as a payroll processor let alone proof of that
6 fact.

7 THE COURT: Okay.

8 MR. QURESHI: So if your Honor would like, I can do
9 that. If your Honor wants to hear from the IRS first,
10 however --

11 THE COURT: Let me hear from the IRS first.

12 MR. QURESHI: Okay.

13 THE COURT: Okay.

14 MS. LOWE: Good morning, your Honor. The debtors say
15 that Kahre's company was strictly a subcontractor. However, as
16 debtor's counsel has pointed out, there was a criminal trial in
17 which Mr. Kahre was prosecuted.

18 And one of the elements that he was indicted for was
19 conspiracy, and this conspiracy was to defraud the
20 United States by dishonest means for purposes of impeding,
21 impairing, and defeating the lawful collection and assessment
22 of Internal Revenue taxes. Those taxes were both income taxes
23 and employment taxes.

24 The manner of the conspiracy was this payroll-service
25 company that he -- those payroll-service process that he sold

1 to other contractors. There was a total of between -- there
2 was a total of 35 contractors which participated in this
3 process.

4 In the trial testimony, numerous times, witnesses
5 testified to that process. They testified that Bravo was one
6 of those contractors that used this payroll-service process.

7 It has been established in the criminal trial, and that is
8 what he is found guilty of is using this payroll-service
9 process, and this process that he sold to other contractors
10 which participated.

11 And in addition, they have submitted the declaration
12 of Dean Griffiths which is not inconsistent with that
13 scenario.

14 Mr. Griffiths states in his declaration that Bravo became
15 concerned with its ability to handle administrative and
16 recordkeeping requirements from its growing employment, so it
17 was that process which then was transferred over to Kahre to
18 pay some of the Bravo employees.

19 He said it was an administrative burden, the payment
20 obligations, and so that is exactly what Bravo did. It
21 transferred numerous of its employees over to Kahre to
22 participate in Kahre's payroll-service company.

23 All of the witness testified to the exact nature of
24 Kahre's relationship to the contractors. We have submitted
25 some of that testimony in support of the IRS claim.

1 The debtors have not to this date objected to the amount
2 of the claim. They're just objecting to the fact that they
3 have to pay the claim.

4 A taxpayer ultimately is responsible for employment
5 taxes. And these employment taxes, you cannot delegate that
6 duty away.

7 There was a payroll-service company. The payroll-service
8 company did not pay them. And as the cases I've cited in my
9 response to their objection to claim, you can't delegate that
10 away. The employer is ultimately responsible for the payment
11 of those taxes.

12 THE COURT: Now, if it was truly a subcontractor that
13 provided labor, you agree that Rhodes is not liable.

14 MS. LOWE: I think we would actually then have to
15 look at all the indices, and, many times, subcontractors are
16 still found liable for employment taxes, so we would have to
17 look at all the specific nature of what -- frankly, they have
18 not submitted any evidence other than Mr. Griffiths'
19 declaration in support of the subcontractor relationship.

20 And even there in that declaration, it supports the fact
21 that they were transferring over to Bravo the recordkeeping and
22 administrative requirements for the employees of Bravo. They
23 admitted those were Bravo employees that were transferred over
24 onto Kahre's payroll system.

25 And as Courts have regularly held, in a payroll-service

1 type process, ultimately, the employer is the one responsible
2 for the taxes, and that cannot be delegated away. It is a
3 responsibility that remains with the employer.

4 It doesn't matter if the payroll-service company fails to
5 pay it. The action then is against that company to not pay the
6 taxes.

7 THE COURT: Now, Mr. Griffiths' affidavit says,
8 "Bravo engaged Pacific as a subcontractor to provide laborers
9 to work on Bravo's building projects."

10 MS. LOWE: And then he says that the laborers
11 provided were the Bravo employees themselves, former Bravo
12 employees, so what they did is they transferred over a number
13 of their employees to the Kahre payroll service.

14 And he states in paragraph 3, "Bravo became concerned with
15 the ability to handle administrative and recordkeeping
16 requirements for its growing employment."

17 What they were transferring over to Kahre is their payroll
18 service function, and it's consistent with what was found at
19 the criminal trial of Robert Kahre. He was operating a payroll
20 service for at least 35 other contractors in the area.

21 And this was found in a court with a jury. They found him
22 guilty of providing this payroll-service company. He was
23 charging the contractors for it. He didn't pay the payroll
24 over, and it is now due, and it is Bravo's responsibility.

25 THE COURT: Okay. All right. Response.

1 MR. QURESHI: Thank you, your Honor. A couple of
2 points. Counsel says that there was testimony in the criminal
3 proceeding that Bravo used UPC as a payroll processor.

4 Respectfully, your Honor, that's not the case. That is
5 an implication that the IRS seeks to draw from that
6 testimony.

7 Nowhere in that testimony is it directly stated by any
8 witness that that is the case. There is general testimony
9 about 35 companies that used these services.

10 Now, your Honor, it's important also to look at the
11 Department of Justice's own press release issued following the
12 conviction by the jury of Mr. Kahre, and that is attached to
13 our objection. It's Exhibit B at Docket 1377.

14 And in that press release from the Department of Justice,
15 they say the following, your Honor: "Between 1997 and 2003,
16 Kahre owned and operated six construction businesses in the
17 Las Vegas area." It goes on to list the six, one of which is
18 UPC.

19 THE COURT: Well, now talk about admissible evidence.

20 MR. QURESHI: Well, a fair point, your Honor, and --

21 THE COURT: I could --

22 MR. QURESHI: And, again --

23 THE COURT: Wait. If we do that, we got every
24 article in the RJ --

25 MR. QURESHI: Well --

1 THE COURT: -- as evidence in this case. I --

2 MR. QURESHI: And I'm happy, your Honor, to strictly
3 apply the Rules of Evidence here because there is no question
4 that the entirety of those trial transcripts are inadmissible.

5 They're hearsay, and there hasn't even been an argument,
6 your Honor, that there's some kind of an exception to the
7 hearsay rule that applies here.

8 Now, your Honor, if I may? One other point which is
9 counsel suggested that the debtors have not objected to the
10 amount of the claim. Also, not true, your Honor.

11 We do object. We say so in our objection. Our issue is
12 that in addition to the principal amount the IRS is seeking
13 penalty interest.

14 Penalties, my understanding, your Honor, is those are
15 penalties that in order to be imposed require a knowing and
16 intentional withholding of taxes that are owing to the IRS.
17 There's not even an allegation that Bravo knowingly did
18 anything here.

19 And, again, just to return one last time and if your Honor
20 will indulge me, I'm happy to go through the details. But line
21 by line, the evidence, the trial transcripts, the inadmissible
22 trial transcripts to which the IRS points as evidence that UPC
23 was a payroll processor, those excerpts, they just don't say
24 that, your Honor.

25 It's an implication that they would like this Court to

1 draw. It's not surprising given that there are 35 companies
2 that were wrapped up in this scheme.

3 The closest they come, your Honor, in the testimony they
4 cite is to say that some -- there is testimony that says -- I
5 believe it's by a Mr. Rodriguez (phonetic) -- that some workers
6 of Bravo were paid in gold and silver coins.

7 It does not say in that excerpt, your Honor, whether those
8 workers were employees of UPC or whether those workers were
9 employees of Bravo, and that, your Honor, is the best they can
10 do.

11 All of the other excerpts are merely general statements in
12 which the nature of the scheme is described in great detail.
13 But without even an implication let alone a direct statement,
14 that Bravo used UPC as a payroll processor.

15 The DOJ's press release makes clear -- and the trial
16 transcripts to the extent your Honor let's them in which,
17 again, we don't think they should be let in.

18 But if they are, those trial transcripts also establish
19 that in addition to this payroll service that, indeed,
20 Mr. Kahre fraudulently sold to other entities they also had
21 construction companies through which they provided laborers,
22 hundreds of laborers. That's what's in their press release.
23 That is entirely consistent with Mr. Griffiths' testimony.

24 And Mr. Griffiths by the way does not say in his
25 declaration, your Honor, that all of Bravo's employees were

1 transferred to UPC, and that's all there was.

2 He says Bravo could not keep up with the demand for
3 laborers. They hired UPC to provide laborers. And once that
4 was done with Bravo's consent, Bravo then took its existing
5 laborers, transferred those employees to UPC such that they
6 became employees of UPC with the exception of managers and
7 supervisors for whom Bravo continued to appropriately I might
8 add withhold payroll taxes.

9 Now, your Honor, we also submitted a declaration from
10 Mr. Bono. That also is attached to our objection at
11 Docket 1377.

12 And what that declaration says, your Honor, is that we
13 went back and I believe actually got these records from the IRS
14 to look at the payroll taxes and records that were filed by
15 Bravo during this period.

16 And what it shows, your Honor, is that Bravo continued to
17 pay and withhold payroll taxes as it was obligated to do, and
18 so that fact, your Honor, is entirely inconsistent with the
19 theory of the IRS.

20 If Bravo was trying to pass off to UPC its payroll
21 processing function, well, it doesn't make sense that it would
22 then continue to do that very thing, process payroll and
23 withhold payroll taxes. But, in fact, we have uncontradicted
24 evidence that that's what they did.

25 So, again, if your Honor strictly applies the

1 Rules of Evidence -- and there's no reason not to -- there is
2 no factual dispute here. There is no evidence that contradicts
3 Mr. Griffiths' testimony.

4 Even if your Honor let's in the transcripts, your Honor,
5 those transcripts simply do not establish anything to refute
6 what Mr. Griffiths clearly says in his declaration.

7 THE COURT: Okay. All right.

8 MS. LAHAIE: Your Honor, I apologize. Could I confer
9 briefly with Mr. Qureshi?

10 (Colloquy not on the record.)

11 MR. QURESHI: That's fine, your Honor.

12 THE COURT: Okay. I'm going to -- it seems to me
13 there's a general issue of material fact. I don't think that
14 Mr. Griffiths' affidavit is sufficient to establish as a matter
15 of law that UPC was merely a payroll company.

16 And even then as Ms. Lowe indicated, there may be
17 circumstances in which a company could be liable, so this needs
18 an evidentiary trial.

19 And I think we should bifurcate, first, as to whether
20 Bravo (sic) was -- I'm sorry -- whether UPC was a subcontractor
21 which merely provided payroll or a subcontractor who provided
22 labor as well as payroll.

23 Then if I determine that they provided merely payroll,
24 then we could have a separate evidentiary trial as to the
25 penalty and interest portion, the willing and knowing, so we

1 don't need to go into that in the beginning.

2 First, it is strictly a limited issue, were they the
3 subcontractor for merely payroll or the subcontractor for
4 labor.

5 Question, do you want -- I doubt you could do a settlement
6 conference. Do you want a settlement conference? That's a
7 little difficult with the IRS issues, but I can give you one if
8 you want.

9 (Colloquy not on the record.)

10 MS. LOWE: No.

11 THE COURT: No? Okay. So do you want to go to trial
12 in March?

13 MR. QURESHI: Your Honor, may I raise one point
14 before we get to dates? Would it be appropriate just to
15 streamline things for us to brief the question of the
16 admissibility of these trial transcripts?

17 THE COURT: I'm relying on Mr. Griffiths' affidavit
18 alone. I'm going to assume --

19 MR. QURESHI: Okay.

20 THE COURT: -- they're inadmissible at this point.

21 MR. QURESHI: Okay. Thank you.

22 THE COURT: I just find his affidavit is just a
23 little bit too ambiguous for me, and --

24 MR. QURESHI: Okay.

25 THE COURT: And nothing he can say can fix it, and I

1 think that's because there are genuine issues of material fact.
2 I mean, this is an area in which, you know, those lines are
3 crossed. I mean, it sounds like they may have provided some
4 payroll and some -- so it's a genuine issue of material fact.

5 MR. QURESHI: Right. But to be clear, your Honor, as
6 to what the factual issue is, it's not whether they were a
7 subcontractor for payroll services versus laborers.

8 If they are, in fact, a subcontractor as I understand the
9 way it works, the laborers are the employees of UPC and not of
10 Bravo, and UPC provides those laborers and, in turn,
11 workers' compensation, et cetera, and then it also has the
12 obligation to remit taxes on behalf --

13 THE COURT: Well, you --

14 MR. QURESHI: -- of those employees.

15 THE COURT: You could still be a subcontractor for
16 one point. You could be a subcontractor to provide payroll and
17 administrative.

18 MR. QURESHI: Fair enough.

19 THE COURT: We're saying the same thing.

20 MR. QURESHI: Okay. As far as the date, your Honor,
21 we'd be pleased to do it earlier if that was possible. But if
22 not, March, certainly.

23 THE COURT: How long do you need to finish doing
24 discovery and how long do you think a trial would take?

25 MR. QURESHI: Well, your Honor, based on our

1 knowledge today of witnesses, I would think it's a single day.

2 THE COURT: Okay.

3 MR. QURESHI: And as far as discovery goes --

4 THE COURT: I can't see how --

5 MR. QURESHI: -- I cannot --

6 THE COURT: I mean, you've fooled around with this
7 for six months now. I don't see how you're going to be ready
8 for trial before March. But if you think you are, fine.

9 I mean, you claim that there aren't any witnesses around,
10 and now you say you're going to go to trial and bring those
11 witnesses.

12 Oh, and by the way, I find Mr. Bono's affidavit to be
13 somewhat useless, so the point being he basically says I don't
14 know anything, and these are my opinions, so it's somewhat
15 useless.

16 (Colloquy not on the record.)

17 MS. LOWE: Your Honor, we would like -- a trial in
18 March is fine with us.

19 (Colloquy not on the record.)

20 THE COURT: I mean, I could do January, but will you
21 be ready by January? This is October, already.

22 MR. QURESHI: Your Honor, I guess -- again, first of
23 all, the reason for the delay is there had been settlement
24 discussions that unfortunately didn't go anywhere.

25 I guess the difficulty is that this is all ten years ago,

1 and so we do have a genuine issue with finding people that were
2 involved. We --

3 THE COURT: So I don't get why you want to go to
4 trial earlier since you can't find your witnesses. That
5 doesn't quite make sense --

6 MR. QURESHI: March is fine --

7 THE COURT: -- to me, but --

8 MR. QURESHI: -- your Honor.

9 THE COURT: Okay. Let me do the week of March 5th,
10 and I may have Judge Thurman who's assisting us on matters do
11 the trial or I may do it. I'll confer with him and see how our
12 calendars go, so we'll do it March 5th.

13 And, pretrial, let's have a pretrial hearing on
14 January 31st, and that can be telephonic for everyone, and have
15 your pretrial briefs (sic) in by -- sorry -- pretrial
16 statements in by January 26th.

17 In this one, I think it will be very helpful to have
18 pretrial briefs as well in beforehand, so that as I'm going
19 through the evidence I can see, well, what is the law in this
20 regard, what's the dividing line between merely a payroll and
21 merely a laborer. Okay.

22 Thank you.

23 MS. LOWE: Thank you.

24 MR. QURESHI: Your Honor, I'm sorry. Is there a time
25 of day for --

1 THE COURT: Oh, excuse me.

2 MR. QURESHI: -- the status conference --

3 THE COURT: I apologize.

4 MR. QURESHI: -- on --

5 THE COURT: Yes.

6 MR. QURESHI: -- the 31st?

7 THE COURT: 9:30.

8 MR. QURESHI: Thank you.

9 THE COURT: Let's make it 10:00 since that is
10 probably -- or 10:30?

11 THE CLERK: 10:30?

12 THE COURT: Don't you think that makes sense because
13 the 9:30 matters seem to take forever?

14 THE CLERK: Sure. We'll do it at 10:30 --

15 THE COURT: Okay. 10:30.

16 THE CLERK: -- then.

17 MR. QURESHI: Thank you.

18 THE COURT: Okay. Thank you. All right.

19 Now let's go to the -- and, Ms. Lowe, you can certainly
20 stay or you can be excused, whatever you wish.

21 (Colloquy not on the record.)

22 THE COURT: All right. Next, let's go to Greenway.

23 MS. LAHAIE: Good morning, your Honor.

24 Meredith Lahaie, Akin, Gump --

25 MS. CHO: And, your Honor --

1 MS. LAHAIE: -- Strauss --

2 MS. CHO: -- it's Shirley Cho. May I be excused as
3 well?

4 THE COURT: Yes.

5 (Thereupon, Shirley Cho, Esq., was excused
6 at 11:13:40 a.m.)

7 MS. LAHAIE: -- Akin, Gump, Strauss, Hauer & Feld,
8 for the reorganized debtors.

9 THE COURT: Okay.

10 MR. HAGUE: Good morning, your Honor. David Hague on
11 behalf of James Rhodes of Fabian & Clendenin.

12 THE COURT: Okay. All right. Go ahead.

13 MS. LAHAIE: As your Honor may recall, we were last
14 here before you with respect to the first half of the
15 reorganized debtor's claim objection as it related to the
16 Greenway Partners claim, and the Court had deferred
17 consideration of the scheduled claims.

18 Before I move into the substance of my argument on the
19 scheduled claims, your Honor, there's one matter I'd like to
20 address.

21 And that is shortly before court began this morning when
22 my colleague and I were on the way to court, we received
23 notification that a further declaration had been filed just
24 this morning.

25 It's unclear what matters the declaration relates to.

1 Although based on the facts, it may relate to both the Greenway
2 claim and the first of the three scheduled claims.

3 I've also advised your Honor that opposing counsel does
4 not have copies, although I will say that I have read the brief
5 contents of the declaration.

6 But, your Honor, at this point in the process, we have
7 been through two rounds of briefs on this claim objection, one
8 in 2010 and one that took place over the summer.

9 At which point, both sides submitted briefs and
10 declarations and whatever other materials they thought may
11 advance their argument.

12 And, your Honor, the reorganized debtors at this point
13 have to object to Mr. Rhodes' last-second Hail Mary litigation
14 strategy that has typified his actions in connection with this
15 matter. We simply do not think it's appropriate for the
16 declaration to be considered at this time.

17 THE COURT: Okay.

18 MS. LAHAIE: I don't know if you want to deal with
19 that matter first, your Honor.

20 THE COURT: Well, I'll strike the declaration, too
21 late.

22 MS. LAHAIE: Your Honor, before I move into the
23 scheduled claims, I believe there was one matter that was still
24 outstanding from the end of our last hearing, and that related
25 to one evidentiary matter with respect to the Greenway claim.

1 And that was Mr. Anderson's allegation that the
2 Main Amundson report which forms the basis of a number of
3 Rhodes' arguments that that document should be admitted under
4 one of the hearsay exceptions to the Federal Rules of Evidence,
5 and, your Honor, I believe that the specific exception that was
6 cited was the business-records exception.

7 Your Honor, I can speak to the rule itself, and I can read
8 the rule into the record, and, obviously, your Honor is I'm
9 sure familiar with the rule and knows that the simple fact that
10 Mr. Anderson stated that that rule and his belief would make
11 the Main Amundson report admissible Mr. Anderson has not met
12 any of these requirements that are, you know, contained within
13 that rule.

14 He has not submitted any evidence as to whether or not the
15 Main Amundson report was prepared in the ordinary course of
16 business as would be required under the Rule of Evidence.

17 We don't think it's applicable, and, your Honor, I'm happy
18 to address it further or submit something in addition if you
19 feel that it's necessary.

20 THE COURT: Okay. All right.

21 MS. LAHAIE: Your Honor, that brings us, then, to the
22 scheduled claims which are on for today. Your Honor, the
23 reorganized debtors in a number of their submissions have
24 included a chart that may assist the Court as I go through my
25 argument, and I can direct your Honor to one of those

1 instances.

2 It's in Docket No. 1466 which is the reorganized debtor's
3 objection, and there is a chart that appears on page 10 of that
4 document that sets forth the three scheduled claims --

5 THE COURT: Okay.

6 MS. LAHAIE: -- and a short recitation of the
7 reasons why the reorganized debtors believe those claims to be
8 invalid.

9 At the outset, your Honor, I will note that the
10 reorganized debtors believe that we do have authority to amend
11 the schedules, and we're seeking, obviously, a declaration from
12 this Court that you agree with that. And to the extent that
13 you don't, we're seeking to have these claims disallowed.

14 So, your Honor, that brings us to the first of the
15 scheduled claims which is a claim asserted by Rhodes against
16 Rhodes Homes Arizona in the amount of approximately \$151,999.

17 Your Honor, this claim ties very closely to the
18 Greenway Partners claim. Mr. Rhodes alleges that he is
19 entitled to this amount as compensation for the fact that he
20 had to advance funds to certain of the debtor's employees.

21 Again, your Honor, we're in the circumstance that we were
22 in connection with the Greenway Partners claim. There is no
23 evidence. There is no documentation.

24 Rhodes alleges that the mere fact that this claim appears
25 on the schedules should be evidence that this Court should

1 consider that the debtors have conceded to the validity of this
2 claim.

3 However, as set forth in the briefs, your Honor, that is
4 not the case. The debtors have made no such admission, and,
5 again, there is certainly no evidence to support any
6 entitlement on Rhodes' behalf to that claim.

7 And, again, as your Honor may recall in connection with
8 the Greenway arguments, Rhodes himself was in charge of
9 preparing the schedules.

10 And this is, yet again, another instance when Rhodes most
11 likely either himself made that ledger entry or directed
12 someone else to make the ledger entry that reflects \$151,000
13 being owed to him by that company, and, your Honor, that's
14 simply not evidence that this Court should recognize to
15 substantiate that claim.

16 Turning next, your Honor, to the Pinnacle Equipment claim
17 which appears on page 11 of the chart, this is the most
18 substantial of the three claims, and its asserted value is
19 \$557,000.

20 Your Honor, the basis of this claim appears to be a
21 contract that Rhodes alleges existed, but that he has not been
22 able to find and has not been able to produce, and that is
23 referenced to the Main Amundson report, but it is not attached.

24 Your Honor, we've obviously requested the document, and
25 neither party has it within their possession. I can only state

1 that Rhodes has conceded on numerous occasions that the
2 document does, in fact, exist, and that it does govern the
3 parties' understanding with respect to the debtor's usage of
4 that equipment.

5 Now, your Honor, the substance of Rhodes' allegation here
6 is that the debtor entity, that Pinnacle Grading that used the
7 equipment at issue, overutilized that equipment more than what
8 had been contemplated by the parties when entering into the
9 contract.

10 But, your Honor, Rhodes hasn't been able to identify any
11 provision within the contract that he can produce that would
12 enable him to assert some kind of true-up payment or other
13 legally-cognizable basis under the contract that would entitle
14 him to be paid and compensated for amounts that he claims were
15 generated in excess of what is bound by the contract.

16 Saying it differently, your Honor, there is no provision
17 and no alleged provision in this alleged contract that says if
18 the debtors overutilize the equipment that Rhodes will then be
19 entitled to a corresponding claim for that amount.

20 Your Honor, what Rhodes is, in effect, doing is admitting
21 that he struck or at least in his own words and in his own
22 opinion that he struck a bad deal, a bad bargain with the
23 debtor entities, that did not cover the actual usage that the
24 debtors had employed this machine for.

25 And he basically wants to be able to restrike that deal

1 and have this Court impose some kind of equitable arrangement
2 which, your Honor, this Court should not do given that Rhodes
3 himself has conceded the existence of the contract.

4 But he wants to be able to rewrite that deal and to
5 restrike that bargain after he has already admitted that he has
6 executed a document with the debtors that's supposed to govern
7 the usage of that piece of equipment.

8 And, your Honor, Mr. Rhodes cannot have it both ways. He
9 cannot say that on one hand there is a contract that governs
10 the usage of this equipment, but, on the other hand, well, that
11 document isn't really sufficient to protect me and what I think
12 that I'm equitably entitled to, and, your Honor, yet again,
13 Rhodes has not asserted a legally-cognizable justification to
14 those funds.

15 And, lastly, your Honor, is the Sedora Holdings claim
16 which is at the bottom of the chart, and this is a \$167,000
17 claim asserted against Heritage.

18 Your Honor, I should note that Rhodes has referenced a
19 document that he believes contains the lenders' acknowledgement
20 that this claim existed which in some ways substantiates his
21 entitlement to be reimbursed for that portion of litigation
22 expenses.

23 And, your Honor, I'd like if we could to turn to that
24 portion of Rhodes' submission, and I'm looking now, your Honor,
25 at Docket No. 1464-3. This is Mr. Huygens' declaration, and

1 it's attached as an exhibit, your Honor.

2 (Colloquy not on the record.)

3 THE COURT: Hang on. I don't have it for some
4 reason. Wait.

5 (Colloquy not on the record.)

6 MS. LAHAIE: Your Honor, I'm happy to hand up the
7 page I have. I'm not sure I need it to speak from.

8 THE COURT: Yeah. That would be helpful. We have a
9 new system which doesn't work with that.

10 MS. LAHAIE: I'll just read it into the record --

11 THE COURT: Okay.

12 MS. LAHAIE: -- your Honor --

13 THE COURT: That's fine.

14 MS. LAHAIE: -- before I hand it up as well.

15 THE COURT: Yeah.

16 MS. LAHAIE: Your Honor, the reference that
17 Mr. Huygens makes is to a portion of the credit agreement, and
18 it's schedule 4.19 that corresponds I believe to Section 4.19
19 which in the credit agreement is labelled brokers.

20 I won't read the section from the credit agreement, but I
21 will read what I believe Mr. Rhodes had been referring to which
22 is a schedule labelled brokers fees.

23 And it's two lines, your Honor, and it states that, "The
24 borrowers have received oral correspondence in respect of a
25 claim for an alternate transaction fee from Deutsche Bank. As

1 of the date hereof, the borrowers believe that this claim is
2 without merit."

3 And, your Honor, as best as the reorganized debtors can
4 tell, this is the concession that Rhodes is citing to in which
5 the lenders have acknowledged that this litigation has existed.

6 And that, presumably, there have been litigation fees
7 incurred that the reorganized debtors now share a burden to
8 participate in.

9 But, your Honor, as I'm sure you can tell from me reading
10 those two lines into the record, there is no admission, no
11 recognition, no acknowledgement of any litigation, any
12 litigation fees incurred, anything that would substantiate the
13 allocation of litigation expenses across any of the debtor or
14 nondebtor entities.

15 And in no way does this document, your Honor, substantiate
16 any entitlement that Rhodes may have to assert a claim for
17 these litigation fees.

18 And, your Honor, the other point that we make in our
19 briefs -- and I'll make it brief up here as well -- is that the
20 way that the Rhodes entities, both the debtor and the nondebtor
21 entities, were structured it was a pass-through structure, so
22 that anything that was attributable to the debtor entities
23 would have flown up.

24 So to the extent that there would rightly have been --
25 which, again, there's no evidence in the record to

1 substantiate.

2 But to the extent that Rhodes could somehow demonstrate
3 that some portion of these litigation costs should be allocated
4 to Heritage, the fact that Heritage is a pass-through entity
5 and whatever value it does or doesn't have ultimately flowed up
6 to Rhodes in any event, it's irrelevant whether Rhodes actually
7 allocated that value to Heritage in the first place.

8 Your Honor, I have nothing else to add. There are a
9 number of other arguments that Rhodes makes, some of them I
10 alluded to at the beginning of my presentation with respect to
11 Rhodes' position that the reorganized debtors have somehow
12 conceded to the validity of these claims.

13 Those are all set forth in detail in the papers. If
14 your Honor has any other questions, I'm happy --

15 THE COURT: No.

16 MS. LAHAIE: -- to answer them.

17 THE COURT: Thank you. Okay.

18 Opposition.

19 MR. HAGUE: Good morning, your Honor. David Hague on
20 behalf of Jim Rhodes. The reorganized debtors have continued
21 to assert that there is just simply no evidence or no
22 documentation before this Court on any of these claims, the
23 Greenway or the scheduled claims.

24 What is before the Court are several reports. There's
25 declarations. There are W-2s that show that they are employees

1 of the debtor's. There are copies of checks. There's copies
2 of wire transfers.

3 There's books and records that shows reimbursements going
4 to Rhodes because he's made these payments. He's made these
5 payments for compensation.

6 There is a lot of evidence that Mr. Rhodes has put
7 forward before this Court that they haven't done anything to
8 rebut.

9 They haven't asked to take a 2004 examination of any of
10 these individuals. They haven't done any subpoenas. They
11 haven't done anything to even demonstrate that what we've put
12 forward is not relevant.

13 They haven't done anything to even rebut what's in any of
14 the declarations, Mr. Rhodes' declaration or Mr. Huygens'
15 declaration.

16 In their briefs, they have said that if Rhodes puts forth
17 facts or evidence sufficient to establish a claim, then the
18 burden shifts to the debtors to show facts tending to defeat
19 the claim by probative force equal to that of the allegations
20 of the proof of claim.

21 And as I have stated, with the Greenway claim and with the
22 compensation claim which is on the Rhodes Home -- I'm kind of
23 trying to talk about those together because it was the same
24 principle -- Mr. Rhodes was making compensation payments to
25 employees of the debtors.

1 This was shown by the W-2s that we have submitted.
2 They're attached to Mr. Rhodes' declaration that show that
3 these were debtor employees.

4 In his declaration, he says, "In order to avoid a
5 disruption in the office, I made these payments to them on the
6 side."

7 I submitted a declaration today which has been stricken
8 that says the same, but that is the arrangement that he had,
9 and there are payments that have come back in to Mr. Rhodes to
10 show and to account for these.

11 Now, on the Greenway one, he wasn't paid about \$800,000
12 for these payments, but I have set forth --

13 THE COURT: Now, Mr. --

14 MR. HAGUE: -- with this Court --

15 THE COURT: There are a number of entities that did
16 not file bankruptcy that Mr. Rhodes held.

17 MR. HAGUE: That --

18 THE COURT: And Mr. Rhodes --

19 MR. HAGUE: That's correct.

20 THE COURT: -- indeed, did not file bankruptcy
21 himself.

22 MR. HAGUE: That's correct, your Honor.

23 THE COURT: Okay.

24 MR. HAGUE: That's correct. But my point is is that
25 these were employed by debtor entities. Coyne, Chin, Stephens,

1 and Hansen were all employed by debtor entities.

2 And I don't know what else we can show this Court other
3 than through declarations that haven't been challenged, through
4 W-2s that haven't been challenged, through checks that haven't
5 been challenged, and through wires that haven't been challenged
6 that are coming from Rhodes accounts --

7 THE COURT: Why couldn't it --

8 MR. HAGUE: -- to these individuals.

9 THE COURT: -- have been a capital contribution, in
10 essence?

11 MR. HAGUE: Why could what?

12 THE COURT: Why wasn't it, in essence, a capital
13 contribution?

14 MR. HAGUE: Well, Rhodes was entitled to a
15 distribution of 2.5 million under the credit agreement, and
16 that's oftentimes how it would work.

17 If he made payments to these individuals, then they would
18 go ahead and subtract what he was owed at the end of the year
19 under this 2.5-million-dollar distribution, but the books show
20 that he did not receive a distribution up to this amount.

21 Now, he paid over \$2,000,000 worth of wages to these
22 individuals and was reimbursed about 1.2 million, but that's
23 the arrangement they had in the office.

24 And they keep talking about no agreement and no contract.
25 Well, there was performance. These individuals worked for

1 several years.

2 It's in Mr. Huygens' declaration. It's in Mr. Rhodes'
3 declaration, and no one has done anything to rebut that
4 testimony. I mean, talk about, you know, genuine issues of
5 material fact.

6 If these were employees of the debtor which no one has
7 fought about and if, in fact, he made these payments to them
8 outside out of his own pocket, then he is entitled to
9 reimbursement.

10 THE COURT: Why isn't it a gift?

11 MR. HAGUE: Because they did services for the debtor.

12 THE COURT: He can make a gift. It's his companies.

13 MR. HAGUE: Yeah. But that's not what he has stated
14 in his declaration, so we now know there's not a gift. These
15 are facts. These are facts --

16 THE COURT: Well, sure. After the fact, he does it.

17 MR. HAGUE: No. This happens as he goes through.
18 That's why he has already been reimbursed 1.2 million.

19 THE COURT: And he wants even more money.

20 MR. HAGUE: He wants what he paid out, your Honor.

21 THE COURT: He wants even more money.

22 MR. HAGUE: Your Honor, you may not like the
23 situation. I understand that, but I'm just telling you what we
24 have submitted and what they have failed --

25 THE COURT: After he --

1 MR. HAGUE: -- to even rebut.

2 THE COURT: -- sneakily --

3 MR. HAGUE: I'm sorry?

4 THE COURT: After he goes around his own company to
5 pay these people --

6 MR. HAGUE: Your Honor --

7 THE COURT: -- how is that equity?

8 MR. HAGUE: Your Honor, he was --

9 THE COURT: How does he have clean hands?

10 MR. HAGUE: He was the --

11 THE COURT: You're asking for equity. How does he
12 have clean hands?

13 MR. HAGUE: Well, I'm not even necessarily -- I'm
14 asking for more than equity. I'm asking for something that's
15 just built into a contract pretty much and performance.

16 THE COURT: Why didn't he write --

17 MR. HAGUE: Now, you're asking --

18 THE COURT: -- a contract?

19 MR. HAGUE: I'm sorry?

20 THE COURT: Why didn't he do a contract?

21 MR. HAGUE: Why did he need to do a contract if there
22 was performance? You're asking that why they did this around
23 his companies.

24 Your Honor, he was the companies. He was the nondebtor.
25 He was the debtor. He was the CEO. And as the CEO and the

1 director and the sole shareholder, he has 100-percent right to
2 be able to say this is the type of arrangement we're going to
3 do.

4 I'm going to employ you, but guess what? There's a whole
5 bunch of other folks in this office --

6 THE COURT: I want to cheat.

7 MR. HAGUE: There's a whole bunch of other folks in
8 this office who are going to want to cheat up their amount that
9 they're owed.

10 They're going to come and say, hey, what about us. We
11 just found out he's making this amount of money through his
12 W-2, so what does he do because -- give you an example.

13 Chris Stephens, he was in charge --

14 THE COURT: So he chooses --

15 MR. HAGUE: -- of entitlements.

16 THE COURT: -- to employ them on his own.

17 MR. HAGUE: So he chooses to pay them on his own for
18 the work they were doing for the debtors --

19 THE COURT: Which helped him as well.

20 MR. HAGUE: -- which helped the debtors.

21 THE COURT: Which helped him.

22 MR. HAGUE: I guess if you're saying they're one
23 economic unit, and he is benefiting the exact same way the
24 debtors are.

25 But we're talking about a proof of claim for amounts that

1 he paid the benefit of the debtors, and I'm just talking
2 strictly on the Greenway and the Rhodes Home Arizona.

3 I mean, we've given stacks and stacks of evidence, and
4 they're clamoring for more evidence, and we don't know what
5 else to provide.

6 I think at the very least, though, there's issues of
7 material fact whether or not these employees then were employed
8 or whether or not they did work strictly for the debtors.

9 Now, it says it in the declaration which no one's
10 challenged, but I don't see how we can simply just resolve an
11 issue and call this a clear legal issue when there's this many
12 facts before the Court. If your Honor would like, I'll move on
13 to the other two in the scheduled claims.

14 THE COURT: Okay.

15 MR. HAGUE: I think I've kind of tackled the Greenway
16 and the Rhodes Home Arizona.

17 The Pinnacle Grading, your Honor -- and we still haven't
18 really addressed the Main report. I understand that counsel
19 has objected to it on the basis of hearsay.

20 But that report was done strictly for the purpose of going
21 in to sort out what was going on between Rhodes, the debtors,
22 and the nondebtors, basically, to determine whether or not it
23 was fair the way things were allocated. There was over
24 \$500,000,000 of intercompany loans.

25 And so the Main report comes in, and the reason that

1 that's created is because they wanted to basically make sure
2 that everything was done in a fair manner and allocate it
3 properly.

4 Now, under the equipment and the grading arrangement that
5 happened, they were supposed to pay lease payments. And,
6 instead, they paid the note payments, and the note payments
7 were less than the lease payments. They overused the
8 equipment. The equipment depreciated, and there was a loss.
9 It's as simple as that.

10 Now, it's not Rhodes as the individual that's claiming
11 this. This is one of his entities that's claiming that they
12 were hurt by the fact that this company did not pay what was
13 due under the lease. They paid the note payments.

14 THE COURT: But we don't have the lease.

15 MR. HAGUE: No. We don't have a lease.

16 THE COURT: Got it. Well, isn't it convenient that
17 you say the lease says that they're entitled to overutilization
18 without a lease?

19 MR. HAGUE: Yeah. I understand your point. There's
20 no lease. We've tried to find it. Mr. Rhodes says there's a
21 lease. The prior CFO in the office says there was a lease.
22 The attorney said that he created a lease, and I cannot find
23 it, your Honor.

24 THE COURT: Okay.

25 MR. HAGUE: Under the last one which is the

1 Heritage Land -- and that's for the one owed to Sedora -- this
2 one again, your Honor, is quite simple.

3 Several entities including Rhodes were sued by
4 Deutsche Bank under an exclusivity agreement which later became
5 as what -- Credit Suisse later was the one who became the
6 actual lender, and so Deutsche Bank sued several of these
7 entities, including Rhodes.

8 And Sedora who was not in the credit facility and who
9 was not sued ended up fronting a lot of these litigation
10 payments.

11 And so this is simply just a reimbursement for funds that
12 were paid to the law firm that was retained in New York to
13 fight this off.

14 THE COURT: Wasn't Sedora part of the lawsuit or no?

15 MR. HAGUE: No. No. Sedora is a nondebtor entity.
16 It was not a part of the lawsuit to my understanding, and,
17 again, we have submitted, your Honor, books and records of the
18 debtor that show that the debtors made quite a few of these
19 litigation payments.

20 But there was a screwup in accounting, and so Sedora ended
21 up making, you know, \$150,000 or so of these payments on behalf
22 of the debtors, but they had no say in this litigation. They
23 weren't sued.

24 In fact, Rhodes eventually was dismissed from the lawsuit,
25 and so what you have is just simply again a reimbursement of

1 costs that were done by, one, a nondebtor entity or a debtor
2 entity, and, I mean, that's how you get to the claim under the
3 Heritage Land and the Sedora. It --

4 THE COURT: Okay.

5 MR. HAGUE: Does your Honor have any questions --

6 THE COURT: No.

7 MR. HAGUE: -- for me on these?

8 THE COURT: Thanks. All right.

9 Response.

10 (Colloquy not on the record.)

11 MS. LAHAIE: Your Honor, I'll be very brief. I think
12 your Honor has a very good grasp of the legal issues that are
13 at stake here.

14 And I think that your Honor has hit the nail on the head
15 with respect to the Greenway Partners claim in the first of the
16 scheduled claims, and, your Honor, I also think that opposing
17 counsel and I are talking past each other a little bit here.

18 Your Honor, we are not contesting the fact that there has
19 been evidence produced in connection with these claims, and,
20 again, we have not contested the admissions made in the
21 declaration.

22 And, your Honor, the reorganized debtors are not
23 contesting the fact that these individuals are employees of the
24 debtors.

25 We're not even contesting the fact at this point,

1 your Honor, that these payments were made to these individuals,
2 and that, your Honor, is the sum and substance of the evidence
3 that has been produced on these claims.

4 And, your Honor, what has not been produced and what
5 cannot be produced because it does not exist is a contract or a
6 document or a legally-binding instrument that would demonstrate
7 both that Rhodes has a legal obligation to pay these
8 individuals and then that the reorganized debtors have a legal
9 obligation to reimburse Rhodes.

10 THE COURT: Well, what about his argument that
11 performance creates the contract?

12 MS. LAHAIE: Your Honor, there has been no evidence
13 whatsoever that the performance that was undertaken by these
14 individuals was done for the benefit of the debtor entities
15 themselves.

16 Your Honor, it's my understanding that these individuals
17 performed services both for the debtors and for the nondebtor
18 entities, and --

19 THE COURT: Why doesn't that create a factual issue
20 as to Greenway? If they perform, if there was performance and
21 if they did work for both, why doesn't that create a factual
22 issue as to allocation or whether or not there was a contract?

23 MS. LAHAIE: Your Honor, I will admit if there had
24 been a contract and otherwise a legally-binding obligation
25 owing on the part of Rhodes or the reorganized debtors to these

1 individuals or to Rhodes, respectfully, then there may be some
2 kind of factual distinction as to how those allocations should
3 be made and what portion of those fees should ultimately be
4 paid to Rhodes.

5 THE COURT: Well, did the Rhodes entities pay some of
6 the Greenway amounts and did they reimburse Mr. Rhodes for some
7 of those amounts?

8 MS. LAHAIE: My understanding, your Honor -- I can
9 confer with Mr. Bono who is here in the court. My
10 understanding is that those amounts were paid by Rhodes. Let
11 me just step back, your Honor.

12 Prior to the petition date, I understand that the debtors
13 paid these individuals whatever their salary had been in
14 accordance with what was typical for the company, i.e., what
15 all the other employees were aware that these individuals were
16 making.

17 And that based on my understanding Rhodes had negotiated
18 undocumented understandings and arrangements with these
19 specific individuals.

20 And the purported justification was so that the employees
21 would not be upset or otherwise frustrated by these payments
22 which then your Honor may question whether these were
23 (indiscernible) market payments to begin with these other
24 payments to these individuals.

25 And Rhodes made -- you know, it's impossible for me to say

1 whether he made all of the payments that he had allegedly
2 promised these individuals --

3 THE COURT: No. Going backwards.

4 MS. LAHAIE: -- that he would make.

5 THE COURT: Was there performance by Rhodes entities
6 repaying Rhodes and/or Greenway?

7 (Colloquy not on the record.)

8 THE COURT: In other words, was there, indeed,
9 performance which can show there is a contract or are you
10 denying there was any performance?

11 MS. LAHAIE: My understanding, your Honor, is that
12 the Rhodes entities did not reimburse Rhodes for any portions
13 of these payments if that's the question that you're asking.

14 THE COURT: And counsel said --

15 MS. LAHAIE: But --

16 THE COURT: -- the opposite.

17 MR. HAGUE: Yes, your Honor. Absolutely.

18 THE COURT: Okay.

19 MS. LAHAIE: Your Honor, if I could confer briefly
20 with my client?

21 THE COURT: Okay.

22 (Colloquy not on the record.)

23 MS. LAHAIE: Your Honor, unfortunately, I don't have
24 that information.

25 THE COURT: Okay.

1 MS. LAHAIE: But based on my understanding, those
2 payments had not been made, but, unfortunately, we can't say
3 definitively at this time.

4 THE COURT: Okay.

5 MS. LAHAIE: But, your Honor, it remains the
6 reorganized debtor's position that without a legally-binding
7 document or agreement --

8 THE COURT: Well, but the Statute of Frauds doesn't
9 require a written contract. I mean, it requires a contract,
10 but a contract can be shown by acceptance, offer, or
11 performance. I mean, there's no Statute of Frauds, right?

12 MS. LAHAIE: Your Honor, I admit I haven't looked
13 closely at that issue.

14 THE COURT: Okay.

15 MS. LAHAIE: But it certainly hasn't been raised by
16 the Rhodes entities nor have they submitted any evidence that
17 would support the fact that there was some sort of offer and
18 acceptance by both parties.

19 There has been no evidence that this Court has admitted as
20 to what the understanding was of the individuals that Rhodes
21 allegedly had this informal agreement with that would
22 substantiate that kind of claim.

23 THE COURT: Okay.

24 MS. LAHAIE: Your Honor, briefly, with respect to
25 Pinnacle Grading -- and, again, I think your Honor hit the nail

1 on the head with this one, too -- and that there is no lease,
2 and it is very convenient for Rhodes to allege that he is
3 entitled to these sort of makeup or true-up payments under the
4 terms of a document that he acknowledges exists but cannot
5 produce.

6 And, again, your Honor, even Rhodes himself by his
7 opposing counsel's characterization of the Main Amundson report
8 which is -- and I'm paraphrasing maybe a bit, your Honor, here.

9 But opposing counsel characterized it as being strictly
10 for the purposes of determining what was going on between the
11 debtors and nondebtors.

12 And, your Honor, that admission alone I would think means
13 that the Main Amundson report could not possibly be considered
14 a business record that would be exempted from hearsay because
15 it was clearly created for a specific purpose and not in the
16 ordinary course of business.

17 And, your Honor, the reorganized debtors (sic) -- or the
18 Rhodes entities should not be entitled to rely on that as
19 admissible evidence in this court. Unless your Honor has
20 anything further --

21 THE COURT: Okay. And on the actual Greenway claims,
22 he's seeking the money advanced to them. How is that different
23 from --

24 MS. LAHAIE: From the --

25 THE COURT: So on the Greenway claims, I guess

1 counsel is claiming there was performance as to that payment.
2 That they were paid. That he was reimbursed partially for
3 that.

4 Is that correct?

5 MR. HAGUE: May I address it --

6 THE COURT: Yes.

7 MR. HAGUE: -- real quickly? Yes, your Honor. With
8 respect to the Greenway claims as well as the one on the
9 Rhodes Home Arizona, we're talking about the same compensation.

10 We have alleged and through the declaration that he paid
11 over \$2,000,000, and that he was reimbursed 1.2. The same with
12 the lawsuit where he made payments, he has been reimbursed a
13 portion of that, not all of it.

14 THE COURT: Okay.

15 MR. HAGUE: That's the course of performance we're
16 talking, no Statute of Frauds --

17 THE COURT: Okay.

18 MR. HAGUE: -- not the sale of goods.

19 MS. LAHAIE: Your Honor, I will also say that there
20 is some discrepancy amongst Rhodes' own documents as to what
21 amounts he is owed in connection with Greenway Partners' claim
22 and what amounts, if any, had been reimbursed.

23 And so I think from that, your Honor, I think the Court
24 should imply or infer that no such amounts -- your Honor should
25 not give the benefit of the doubt to Rhodes.

1 Your Honor may recall that Rhodes had set forth one amount
2 in his proof of claim with respect to the amounts he believed
3 he was owed in connection with the Greenway Partners, and I'm
4 looking for the exact dollar amount, but it was closer to
5 \$900,000. It was certainly in the \$800,000 range.

6 And in support of Rhodes' own entitlement to those funds,
7 he cites as his primary form of evidence the Main Amundson
8 report.

9 Aside from the hearsay issues associated with that
10 document, the Main Amundson report sets forth a claim somewhere
11 in the realm of \$600,000 that Rhodes is entitled to on account
12 of that claim.

13 So even with respect to Rhodes' own evidence and the
14 evidence he has put forth before this Court, there is no
15 consensus as to what he is owed on account of that Greenway
16 claim.

17 THE COURT: Okay. All right. Thank you. All right.

18 Well, with respect to Greenway and the Rhodes
19 compensation, there is factual issues about whether or not
20 there was a contract.

21 And your briefing didn't really address that issue. You
22 just say there's no written contract. Well, that doesn't end
23 the issue.

24 There doesn't have to be a written contract if there is a
25 contract established by the general principles of contract law,

1 you know, was there a course of performance that shows there
2 was a contract, and that wasn't addressed.

3 So I guess there's a factual issue as to was there a
4 contract for the Rhodes estates to repay Rhodes on account of
5 the compensation.

6 Now, I tend to think that even then there may be other
7 defenses such as you can now recover the money he's repaid
8 because he shouldn't have been paid that.

9 But that's I guess an issue that's all wrapped up in your
10 other litigation as well, so there's a factual issue as to
11 that.

12 I will sustain the objection as to the Pinnacle Grading.
13 There is no written contract. Well, nobody can produce the
14 contract.

15 If there is a written contract, you certainly can't claim
16 quantum meruit which you haven't really alleged, and there's no
17 reason to believe that the contract would have required
18 overusage, so that objection is sustained.

19 The Heritage Land, there is an allegation that there was,
20 of course, a conduct which establishes a contract to repay
21 those amounts. A, was there a contract and, B, to what extent
22 did the estate benefit? Maybe there's a fraudulent transfer.

23 I will sustain the objection to the admission of the
24 Main Amundson report. I do find that's hearsay. So in making
25 my decision, I'm not relying on the Main Amundson report.

1 So I guess we need some scheduling orders to see where we
2 are in getting these things all resolved. Do you want to come
3 back in about a month to let me know where we are?

4 MS. LAHAIE: I think --

5 THE COURT: Do you want a settlement conference
6 again?

7 MS. LAHAIE: Your Honor, we've given that a couple
8 bites at the apple. I'm not sure at this point it would be
9 productive.

10 THE COURT: Okay.

11 MS. LAHAIE: The one thing I will remind, your Honor,
12 if we could move as expeditiously as possible as we can. As
13 your Honor knows, we do have the litigation, the
14 Litigation Trust, that's awaiting the pendency of the outcome
15 of this. I --

16 THE COURT: Well, you're talking about such small
17 amounts now in the scheme of things. Why are we fooling around
18 with this as opposed to just going forward on the other things?
19 I mean, you're now talking about a total of -- well, he asked
20 for 800,000.

21 MS. LAHAIE: And your Honor may also recall that the
22 outcome of the tax claim, Rhodes had taken a timely appeal of
23 that issue, and that appeal is still pending also resolution of
24 this issue.

25 THE COURT: Okay. Well, you tell me when you're

1 ready for trial.

2 MR. HAGUE: Well, just looking at this, there's going
3 to be several witnesses that I think we're going to have to
4 take depositions of, and I would --

5 THE COURT: Why haven't you done it, already?

6 MR. HAGUE: Huh?

7 THE COURT: Why haven't you done it, already?

8 MR. HAGUE: Well, we submitted the declarations of
9 the witnesses that we have. The one that I had today was
10 stricken, and so I'm going to have to probably do that again.

11 THE COURT: I know. Why haven't you taken their
12 depositions before?

13 MR. HAGUE: I --

14 THE COURT: Why have we waited?

15 MR. HAGUE: Because we thought the declarations would
16 be sufficient evidence. They're willing to put forward their
17 testimony. It hasn't been rebutted. That's why we haven't
18 taken --

19 THE COURT: Well --

20 MR. HAGUE: -- their depositions.

21 THE COURT: -- when are you ready for trial?

22 MR. HAGUE: I propose the same time you granted the
23 other one which was only a very simple issue which is March.

24 MS. LAHAIE: Your Honor, I just think that given that
25 that there's a whole basket of litigation that's pending the

1 outcome of this. We just would like to move as
2 expeditiously --

3 THE COURT: Well --

4 MS. LAHAIE: -- as possible.

5 THE COURT: -- look, you guys have continued this
6 thing 20 times, already, so don't blame me because you guys
7 have continued this from like June a year ago. I mean, I
8 appreciate you want to move it fast, but you waited a year.
9 You can have December 5th.

10 MS. LAHAIE: December 5th, your Honor?

11 THE COURT: December 5th.

12 MS. LAHAIE: That's fine --

13 THE COURT: Are you going to be ready --

14 MS. LAHAIE: -- for the reorganized debtors.

15 THE COURT: -- by December 5th?

16 MS. LAHAIE: We can be --

17 THE COURT: If I give you a date --

18 MS. LAHAIE: -- your Honor.

19 THE COURT: -- I want you to be ready. No
20 continuances.

21 MR. HAGUE: We'll be ready, and this is an
22 evidentiary hearing, correct?

23 THE COURT: Evidentiary hearing on whether or not
24 there's a contract -- on the objection to claim on those
25 two issues, the Greenway -- three, Greenway, the Rhodes

1 compensation, and the litigation expenses.

2 We can bifurcate it as to amount, well, and I guess that
3 doesn't make any sense. We need to have it at the same time to
4 know if there was a contract to what extent, if at all, is the
5 estate responsible.

6 And if you intend to amend your lawsuit for a fraudulent
7 conveyance of what he's paid back, already, do it. I mean,
8 maybe what he was paid already is a fraudulent conveyance. I
9 don't see why it wouldn't be.

10 MS. LAHAIE: Your Honor, if I could just ask for one
11 point of clarification also with respect to the Pinnacle claim?
12 You sustained the debtor's --

13 THE COURT: Sustained the objection.

14 MS. LAHAIE: And just to be clear as to procedurally
15 what happened then, we had sought relief, just stricken that
16 from our schedules.

17 My understanding is that once that happens and
18 (indiscernible) do that the Rhodes entities would then have
19 30 days to file a proof of claim. I don't know to what extent
20 we can try to end run that process.

21 THE COURT: I just find there's no merit to the
22 Pinnacle claim.

23 MS. LAHAIE: Okay.

24 MR. HAGUE: Your Honor, we would not file a proof of
25 claim on the Pinnacle. The way I understand it is because the

1 way it was scheduled we never had to file a proof of claim.

2 This serves as their objection. We're not going --

3 MS. LAHAIE: Okay.

4 MR. HAGUE: -- to file --

5 THE COURT: Okay.

6 MR. HAGUE: -- a proof of claim on that.

7 THE COURT: All right. Thank you.

8 MS. LAHAIE: That's all.

9 Thank you.

10 THE COURT: All right. So do you want December 5th
11 for a trial?

12 MS. LAHAIE: We do, your Honor, yes.

13 THE COURT: All right.

14 MS. LAHAIE: Thank you.

15 THE COURT: Is a day sufficient?

16 MS. LAHAIE: Yes --

17 MR. HAGUE: I think one day --

18 MS. LAHAIE: -- your Honor.

19 THE COURT: Okay.

20 MR. HAGUE: -- would be fine.

21 THE COURT: All right. Thank you.

22 THE CLERK: Your Honor, are you going to hear that --

23 THE COURT: I'm sorry.

24 THE CLERK: You're going --

25 THE COURT: I can't hear you.

1 THE CLERK: You're going to hear --

2 THE COURT: Yes.

3 THE CLERK: -- the trial December 5th? Okay.

4 THE COURT: Okay. Thank you.

5 THE CLERK: Thank you.

6 All rise.

7 (Recess at 11:46:54 a.m.)

8 (Court reconvened at 11:49:04 a.m.)

9 THE COURT: Be seated.

10 (Colloquy not on the record.)

11 THE COURT: Sorry. I forgot the motion to quash and
12 look on these shortened times. Just because you're going to be
13 here on a certain day doesn't mean that you think you can
14 shorten time on stuff four days in advance.

15 That's why I put this for a status only. It's nonsense,
16 and it's nuts because we never get good responses when things
17 are on shortened time, so don't do it again. Okay.

18 On the motion to quash, when do you want to argue it? I
19 want a reply. I guess I just got the reply today.

20 MR. HAGUE: Whatever works for this Court. All we
21 would have left to file would be our response, and I know
22 there's other objections now that have objected to this, and I
23 don't know if the Court would prefer to have this all together.
24 I know there's two other parties here today.

25 THE COURT: Yeah.

1 MR. HAGUE: And --

2 THE COURT: That's why I think motions to shorten
3 time in this area are stupid.

4 MR. HAGUE: Your Honor --

5 THE COURT: And they didn't consent to it, either.

6 MR. HAGUE: Your Honor, the only reason we did it was
7 to try to get before the Court, so we could get something laid
8 out because of the extent of the subpoenas.

9 THE COURT: I understand. But to ask for four-days'
10 notice, you knew this was happening weeks ago.

11 MR. HAGUE: Your Honor, we filed the motion for
12 shortening time the day we filed for the subpoena which was
13 immediately. I apologize to this Court, but that's what we
14 did.

15 THE COURT: Okay. All right. Two weeks, is that
16 sufficient? I want responses. I want it all together. Is
17 that sufficient? Let me know.

18 MR. HAGUE: No. I think that we need more time than
19 two weeks.

20 THE COURT: Okay.

21 MR. HAGUE: I'd say a month.

22 THE COURT: Okay. Now, does that affect the
23 discovery for the trial?

24 MS. LAHAIE: Your Honor, you're looking over here,
25 but I believe the matter is being handled by Litigation Trust

1 counsel on the phone. I'm not sure if they're still on.

2 THE CLERK: They're not. I already hung up.

3 MS. LAHAIE: Okay. Your Honor, this is not a matter
4 that Akin, Gump --

5 THE COURT: Okay.

6 MS. LAHAIE: -- is handling.

7 MR. HAGUE: Your Honor, just so I understand, though,
8 if we're on the same page, they have their subpoenas. We have
9 our objection and motion to quash. Other parties do as well.

10 They have filed their reply I think just to my motion to
11 quash, not to these others, and now you're asking that we all
12 file replies within a month and have a hearing here within a
13 month? I --

14 THE COURT: You all have --

15 MR. HAGUE: I don't understand.

16 THE COURT: -- a hearing in month.

17 Well, get them on the phone.

18 (Pause at 11:51:06 p.m.)

19 (Colloquy not on the record.)

20 (Pause concluded at 11:52:33 p.m.)

21 THE COURT: Well, you know, are they back on? No?

22 Also, well, where is the certificate that you attempted to
23 confer in good faith --

24 MR. HAGUE: We filed it with the court.

25 THE COURT: -- before you filed this?

1 MR. HAGUE: Yeah. It was just filed with the court.
2 You're talking about on our motion to expedite?

3 THE COURT: Right.

4 MR. HAGUE: Yeah. It's there.

5 THE COURT: No. Your good faith under the discovery
6 rules.

7 MR. HAGUE: We filed the attorney-acknowledgement
8 form. I thought that's what we were supposed to file.

9 THE COURT: But under the Federal Rules of Discovery,
10 you're supposed to attempt to confer in good faith.

11 MR. HAGUE: We did, your Honor, and we put that in
12 the attorney acknowledgement. We said that we called counsel
13 and asked if they would be willing to have this hearing today.

14 THE COURT: That's a separate issue.

15 MR. HAGUE: Then what issue are you --

16 THE COURT: Under the discovery rules, you're
17 supposed to confer in good faith before you bring motions to
18 quash. Did you do that?

19 MR. HAGUE: Yes, we did. We did it on a call. We
20 had a conference call with them.

21 THE COURT: And did you attempt to resolve anything?

22 MR. HAGUE: Yes, we did. It was with the
23 Litigation Trust, the firm out of Texas.

24 THE COURT: All right. Well, let's set this hearing
25 for next week. When did the other parties file their

1 objections and who filed? I don't see any on -- well, I can't
2 tell. I can't get on.

3 THE CLERK: All right. Thank you.

4 MR. HAGUE: Your Honor, they filed. It's Document
5 No. 1555, and I think it's just in response to --

6 THE COURT: No, no, no, no, no. You told me other
7 entities have now filed objections to the motion to quash. Who
8 else --

9 MR. HAGUE: Oh, I'm --

10 THE COURT: -- has filed one?

11 MR. HAGUE: I believe it's Omaha. Is
12 it --

13 MR. GLOVER: Your Honor, Chet Glover here on behalf
14 of Mutual of Omaha. We filed an objection to the subpoena for
15 the 2004 exam. That's Document 1547.

16 THE COURT: But you didn't file a motion to quash.

17 MR. GLOVER: We did not.

18 THE COURT: Okay.

19 MR. GLOVER: Yeah.

20 THE COURT: So then I don't have your motion on, so
21 there's no motion to quash.

22 MR. GLOVER: Correct, your Honor.

23 THE COURT: Did anybody else file a motion to quash?

24 MR. THOMAS: No, your Honor.

25 THE COURT: All right. Why did you tell me they had?

1 MR. HAGUE: They filed an objection. If I misspoke
2 and said a motion to quash, I apologize. They filed an
3 objection.

4 THE COURT: All right. So we'll have a hearing next
5 week, then. We'll have a hearing on October 5th at 9:30, and
6 I'm going to require presence of counsel, any counsel that
7 intends to argue. All right.

8 Thank you.

9 And I suggest you try and work it out.

10 (Colloquy not on the record.)

11 THE CLERK: All rise.

12 (Court concluded at 11:55:16 a.m.)
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1 I certify that the foregoing is a correct transcript
2 from the electronic sound recording of the proceedings in
3 the above-entitled matter.

4
5
6 /s/ Lisa L. Cline

10/04/11

7 Lisa L. Cline, Transcriptionist

Date